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A Comparative Study of the Takaful Rules and Regulation for Malaysia and Indonesia Act

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ABSTRACT
Nowadays, each country has adopted their own rules and regulation, and it's usually different when we compare one state with another. The same situation applies to the insurance and Takaful industry for ASEAN countries especially Malaysia and Indonesia. Adopting the analysis content methodology, this study intends to analyze the similarities and differences of Takaful rules and regulations between Malaysia by Islamic Financial Services Act 2013 (IFSA 2013) and Indonesia are governed and Undang-Undang No 40 (UU40). IFSA (2013) is a particular Shariah compliance guideline for financial services including Takaful whereas UU40 only focus on Takaful and insurance service. The results of this study could provide a significant contribution to Takaful operators in ASEAN countries especially Malaysia and Indonesia.
Keywords: Takaful rules and regulations, Act, IFSA, Undang-Undang 40, Malaysia, Indonesia

INTRODUCTION

Despite 2011 being a milestone year for global financial regulation implementation, the insurance sector is far from having a reliable and standard set of international regulatory requirements. Nowadays, each country has adopted their own rules and regulation. Thus, harmonization of the rules and regulation among countries needs to take place to enable business are free to cross-border without interference from domestic law of member state. In some countries, the rules and regulations are governed by either government or independent agency. Independent agency is a separate party which is appointed by the government purposely to monitor the Takaful industry.

Rules and regulations are the main essential tools to ensure the perfectness of the implementations of any guidelines. Rules and regulations are a set of principles and visibly commanding rules (Berkem, 2014) based on the behaviour of the market and the principle prudentially (Jean Kwon, 2013) under regulatory supervision that create a situation which represents a significant part in determining what can and cannot be done by the industry (Brophy, 2012).

The same situation applies to the insurance and Takaful industry. In the United States (US), for example, despite the reforms introduced in the 1990s to unify the set of rules, regulation of the insurance market in the US is state based. Every State Regulatory Commission establishes regulations deemed necessary (Castagnolo, 2013). This shows that the rules and regulations are controlled by a government. Similarly, the European Union (EU) also practices a government regulation under the European Commission. The role of the European Commission is described precisely in the Treaty of the European Union and is reinforced by the Commission's house rules. In the European Union, the responsibility to set the legislative agenda is situated to the Commission (Hooghe, 2005). The advent of the European Union has had a further impact due to the desire to create a common market governed by universal principles and harmonize insurers across Europe (Swarup, 2012). In contrast, New Zealand is one of the countries that allowed their independent agency named the Insurance Council of New Zealand to regulate its insurance industry (Castagnolo, 2013).

In Malaysia, both the conventional insurance and Takaful industries are regulated by the Central Bank of Malaysia (BNM) through the Financial Services Act 2013 (FSA 2013) and Islamic Financial Service Act 2013 (IFSA 2013), (Thanasegaran & Shaiban, 2014). Whereas in Indonesia, Undang-Undang No 40 and also POJK No 23 are the law that applies to both conventional insurance and Takaful industry. The Act was issued and control by the Government of Indonesia through its Financial Services Authority of Indonesia (FSAI) and focuses on licensing requirement, Shariah governance and risk assessment (Sukmana & Hidayat, 2014).

LITERATURE REVIEW

The changes in the Takaful industry need to be dynamic, professional and better capitalized (Kirsten, 2007). It also applies in Takaful industry as well. 2011 is a milestone year for a global financial regulation implementation, and it's including Islamic financial sectors. Nevertheless, the Takaful industry is still developing the standard set for the international regulatory requirement to suit with the changes in the world economy. According to Khan and Bhatti (2008), Malaysia and Indonesia are among the Southeast Asian countries which are promoting the most comprehensive and advanced version of Islamic banking and finance in the region.

In the world of the insurance market, Takaful is the fastest growing area which grows at 20 percent to 25 percent per annum compared to the average world growth of conventional insurance which is at 5 percent to 8 percent per annum (Nico & Peter, 2010). It was due to the customers and business demand for the Islamic insurance. Takaful business can attract even non-

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Muslim to their product due to its connection with the Islamic Syariah and not just a system. Its business has an apparent ethical structure which can be marketed to both Muslims and non-Muslims. The substantial rise in the demand for Takaful insurance is due to this ethical nature of the product which attractive to both Muslim and non-Muslim.

The process of globalization will create an open market for all industries including the Takaful industry. Example, the establishment of the ASEAN Free Trade Area (AFTA) allows the Takaful operator from another country to operate in another member country. This will foster an open market in the Takaful industry which requires a set of minimum standard of rules and regulations to protect the industries from misconduct and unethical practices. The initiation of the General Agreement on Trade and Services (GATS) also require the local company to have the ability to compete with world-class companies in the international market. For Takaful industries, it's very crucial for each country to have rules and regulations which will facilitate and increased the competitive advantage to the insurer and also the insured.

According to Ernst and Young (2014), the enhancement of the regulations has opened new opportunities in rapid growth market in the developing country such as Malaysia and Indonesia. The growth of Malaysia Takaful industry contributes about 71 percent of ASEAN gross Takaful contributions in 2014. Among the contributing factors to the progress are the enactment of Islamic Financial Services Act 2013 (IFSA 2013) and the support of Bank Negara Malaysia (BNM) as the regulator of Takaful and insurance industries. BNM as the primary regulator for insurance and Takaful industry in Malaysia set the minimum capital requirement at RM100 million for both life and non-life Takaful operator. Simultaneously, all Takaful operators are subjected to solvency regulation.

In comparison to Indonesia, Malaysia has set a target capital available at the level of 130%. The perspective of policyholder protection under the Malaysia Deposit Insurance Corporation (MDIC) administers the Takaful and Insurance Benefits Protection System (TIPS) which protects specific benefits under life and general insurance. Interestingly, foreign ownership is generally limited to 70% and the amount exceeding 70% must get the approval from BNM on the case to case basis (Sivalap, Chucheep & Arunee, 2014).

Currently, Indonesia adopted Undang-Undang No 40 for both Takaful and insurance companies. The new act of Undang-Undang No 40 covers the aspect of corporate governance, market conduct, consumer protection and licensing. This Undang-Undang also must read together with the POJK No 23. The move is expected to reshape Indonesia Takaful industry by spurring mergers as companies try to meet the capital requirement for their expansion purposes. The Insurance Bureau at the Ministry of Finance (MOF) is the Indonesian regulator for Takaful industry. According to Sivalap, Chucheep, and Arunee (2014), the regulator set the minimum capital requirement, the solvency regulation, policyholder protection and foreign ownership restrictions to protect the industry. Therefore, Indonesia decided that the risk-based capital (RBC) solvency margin ratio of at least 100% and each Takaful operator must form its protection fund to protect the interest of participants. Additionally, regarding foreign ownership restriction, Indonesia's fixed that the foreign shareholders of the entity carrying Takaful activities are limited to 80% at the establishment of the company.

Based on the above discussion, most ASEAN countries including Malaysia and Indonesia had rules and regulations that provide by their regulator to protect the Takaful industry. The regulator is responsible for usually set on a minimum capital requirement, the solvency regulation, policyholder protection, and foreign ownership restrictions. This shows the importance of the rules and regulation to protect the Takaful industry.

ISLAMIC FINANCIAL SERVICE ACT 2013 - TAKAFUL ACT OF MALAYSIA AND UNDANG-UNDANG NO 40 – TAKAFUL ACT OF INDONESIA: A COMPARATIVE ANALYSIS

The current general Takaful rules and regulations are the Islamic Financial Service Act 2013 (IFSA 2013) in Malaysia and Undang-Undang No 40 (UU40) in Indonesia. However, UU40 referring to Takaful company and the conventional insurance company was more straightforward and only discuss on the headlines for insurance and Takaful because the further explanation of it will be provided in the Peraturan Otaritas Jasa Keuangan (POJK). Whereas, IFSA 2013 referred to Takaful company covered all the Takaful rules and regulations and also compiled of banking, Takaful and money market.

Part I (1) in IFSA 2013 and chapter I (1) in Undang-Undang No 40 explain about the definitions of operational terms which is used in Takaful operations. Its include 'approved Takaful broker,' 'family Takaful business,' 'family Takaful certificate,' 'international Takaful business,' 'licensed for Takaful operator,' 'Takaful agent' and others. Part II (2) in IFSA and chapter XIII (13) of Undang-Undang No 40 describe the regulatory objective and power and function of bank and regulations and supervision for Takaful sector. The principal regulatory objectives of these acts are to promote the financial stability and compliance with Shariah. Part III (3) of IFSA 2013 and Chapter II (2), Chapter III (3) and Chapter IV (4) of Undang – Undang no 40 about the authorization which covers the scope of general business for Takaful. In this part, the act discussed the authorized business to be carried on by an authorized person, grant of a license by Minister and licensed for Takaful operator to carry a Family Takaful or general Takaful.

Part IV (4) of IFSA 2013 and chapter VIII (7) of Undang-Undang No 40 explain about Shariah compliance, Shariah governance, and audit and Shariah compliance. Noted from the act that the IFSA 2013 discuss in details about the above matter but UU40 only touch the Syariah compliance on the surface. The topic touched in Undang-Undang No 40 based on articles 36, 37 and 38 respectively. Part V (5) of IFSA 2013 and Chapter V (5) of Undang-Undang No 40 discuss on the payment system based on the designation of payment systems and Islamic payment instruments, the requirement of operation of payment systems and finality of payment. The topics also discussed in Undang-Undang No 40 based on the articles 26 and 31. Part VI (6) of IFSA 2013 and Chapter III (3), Chapter V (5), Chapter VI (6) and Chapter XII (12) explained the prudential requirements. This chapter consists of the standard on prudential matters, corporate governance, transparency requirement, auditors, appointed actuaries, Takaful fund and shareholders fund and subsidiaries.

Part VII (7) of IFSA 2013 and chapter III (3), Chapter IV (4) and Chapter IX (9) of Undang-Undang No 40 discuss the ownership, control and transfer of business. This part is further explained about the transfer of business, reconstruction or amalgamation of a licensed person. Its include approval required for business transfer scheme, orders sought by transferor and transferee and prohibition of payment. Part VIII (8) of IFSA 2013 discuss on the financial groups which cover and explain the safety and soundness of licensed person. It is quite similar to chapter IV (4) of UU40 where it's cover the topic of licensing. Part IX (9) in IFSA 2013 focus on the business conduct and consumer protection as a whole. This part will cover the act on the interpretation of the wording used, explain the business conduct and how to deal with compliant and dispute. This part will touch more on the Takaful issue including the information and secrecy. This part also discusses in details about restriction relating to consumer protection. UU 40 also provide the policy holders protection, insured or participants in Chapter XI (11) but not in details and some in Chapter V (5). The details of the same provided under Bab V (5) POJK No 23 which covered under Insurance Customer Protection.

In IFSA 2013, Part XII (12) and chapter V (5) in Undang- Undang No 40 statements about the business conduct in article 22 and 23. It's also sated in chapter XIII (13) of UU40. In this chapter explain how the bank may examine without prior notice the business and affair of an authorized person, a market participant and approved representative office. Part XVI (14) in IFSA 2013 discuss the intervention and remedial action. In this chapter the winding up process discuss in details include general provisions, the priority of payments and general provisions about actions taken by bank and Takaful operators. In UU40 the similar topics covered under Chapter X (10) under the subtopics of dissolution, liquidation, and bankruptcy.

In IFSA 2013, part XVI (16) and chapter XVI (16) in Undang-Undang No 40 discuss on the penalty and confinement. Its include investigation powers, administrative actions, civil actions and criminal offenses. It's also provided under Chapter XV (15) under UU40. Its further explains under bab VIII (7) under POJK 23. Part XVII (17) in IFSA 2013 and chapter XIII (13) in Undang-Undang No 40 discuss the general provision. This includes the regulation and supervision by the Minister. In this case, the Minister may on a recommendation by the bank be able to make such regulations as may deem necessary.

Lastly, in part XIII (18) in IFSA 2013 and chapter XVIII (17) in Undang-Undang No 40 stated about the transitional matters and provision. It's included conversion to single Takaful business and licensed Takaful operator which is a private company to convert to a public company. In IFSA 2013 the details about repeal, saving and transitional matter is provided. Chapter XVIII (18) in Undang-Undang 40 also discuss on the closing of the Takaful operators. Its further explains under Bab VIII (8) in POJK 23.

The differences between Islamic Financial Services Act 2013 (IFSA 2013), Undang-Undang No 40 and Peraturan Otaritas Jasa Kewangan (POJK 23) have six (6) differences contents between IFSA 2013 and Undang-Undang No 40. There 4 part in IFSA 2013 but not available under Undang-Undang No 40. Nevertheless, this part not related to the Takaful Operators. Part X (10) discuss the Islamic money market and Islamic foreign exchange market. Part XI (11) explains the submission of the document. Part XIII (13) stated the circumstances where the bank has the power to issue directions. Part XV (15) discuss the other power of the bank. These items also not discuss in the POJK 23.

The other three (3) differences are where there is stated in Undang-Undang No 40 but not discuss in IFSA 2013. There are Chapter VIII (8), Chapter XIII (13) and Chapter XIV (14) which discuss on the mandatory insurance programme, regulation and supervision and business association of insurance.

The Malaysian Islamic Financial Services Act 2013 (IFSA 2013) and the Undang-Undang No.40 (UU 40) with Peraturan Otaritas Jasa Keuangan No.23 (POJK 23) of Indonesia contain some remarkable similarities and differences in their provisions. A comparative analysis between the ISFA 2013 and UU40 with POJK 23 is shown in Table 1.

Table 1: A Comparative Analysis of Malaysian Islamic Financial Services Act 2013 (IFSA 2013) and Undang-Undang No.40 (UU 40) with Peraturan Otaritas Jasa Keuangan No.23 (POJK 23) of Indonesia

<table>
<tr><th colspan="5">SIMILARITIES</th></tr>
<tr><th rowspan="2">Criteria</th><th rowspan="2">IFSA 2013
(Malaysia)</th><th colspan="2">UU No 40 & POJK No 23
(Indonesia)</th><th rowspan="2">Remark</th></tr>
<tr><th>UU No 40</th><th>POJK No 23</th></tr>
<tr><td>Definitions of Operational</td><td>Part I (1)
Preliminary
Takaful
- An agreement based on mutual assistance under which Takaful participant agree to contribute to a common fund providing for mutual financial benefits payable to the Takaful participants or their beneficiaries on the occurrence of pre-agreed events.</td><td>Chapter I (1)
General Provisions
Article 1
Shariah Insurance
- A collective agreement which consists of an agreement between the Islamic insurance company and the policyholder to manage the contribution based on Islamic principles to help and protect each other.</td><td>Article 12
The Insurance Policy for Insurance Products with Shariah principles</td><td>Both provisions share similar provisions explaining the definition of terms and operation of Takaful.</td></tr>
</table>

The Regulatory Objective and Power and Function	Part II (2) Regulatory objective and power and function of bank	Chapter XIII (13) Regulations and supervision	Not available	Both provisions explain the regulation and supervision of Takaful business. IFSA authorize the Central Bank of Malaysia to regulate and monitor the Islamic financial services institutions in Malaysia. On the other hand, UU No.40 authorizes the Financial Services Authority (FSA) to regulate and monitor the insurance, Islamic insurance, and reinsurance industry.
General Business for Takaful	Part III (3) Authorization i)Authorized business ii)Restriction on dealing of authorized person iii)Representative office iv) Revocation, surrender or cessation of business or operations. v)General matters	Chapter II (2) Scope of business insurance Chapter III (3) Legal form and ownership insurance companies Chapter IV (4) Licensing	Not available	Both provisions explain the authorization of the Takaful business such as licensing and revocation of business. Chapter II of UU No. 40 enumerates authorization process for both insurance and Takaful business.
Shariah Compliance	Part IV (4) Shariah requirement	Chapter VIII (7)**	Not available	Both provisions discuss about Shariah compliance.

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	i)Shariah compliance ii)Shariah governance iii)Audit on Shariah compliance	Capacity building insurance, Shariah insurance, reinsurance and reinsurance state. Article 36, 37 & 38		
Payment System	Part V (5) i)Designation of payment systems and Islamic payment instruments ii)Requirement of operation of payment systems and issuance of designated Islamic payment instruments iii)Finality of payment and netting arrangement	Chapter V (5) BUSINESS CONDUCT Article 26 and 31**	Not available	Both provisions discuss about Payment system
Prudential Requirements	Part VI (6) Prudential requirements i)Standard on prudential matters ii)Corporate governance iii)Transparency requirement iv)Auditors v)Appointed actuaries vi)Takaful fund and shareholders fund vii)Subsidiaries	Chapter III (3) Legal form and ownership insurance companies Chapter V (5) Business conduct Article 12, 17, 19, 20 and 21** Chapter VI (6) Governance of business insurance, Form of cooperation and business together	Not available	Prudential matters, corporate governance, transparency requirement, auditors, appointed actuaries, Takaful fund and shareholders fund and subsidiaries.

		Chapter XII (12) Professional service provider for insurance companies Article 55**		
Ownership	Part VII (7) Ownership, control and transfer of business	Chapter III (3) Legal form and ownership insurance companies Chapter IX (9) Change of ownership, merger and melting Article 40	Not available	Both provisions discuss the ownership, control, and transfer of insurance and Takaful business.
Licensing	Part VIII (8) Financial groups i)Safety and soundness of licensed person	Chapter IV (4) Licensing	Not available	Both provisions authorize the Central Bank and FSA to exercise oversight over financial groups for the purposes of promoting the safety and soundness of a licensed person.
Consumer Protection	Part IX (9) Business conduct and consumer protection	Chapter XI (11)** Policy holders protection, insured or participants Chapter V (5) Business conduct	Bab V (5) Insurance customer protection (perlindungan konsumen asuransi)	Consumer protection is a priority in both laws. This is clearly discussed in both statutes which regulate the business conduct of the policyholders and the consumers. IFSA discussed in detail in Schedule 7, 8, 9 and 10. POJK discussed in detail in

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				Chapter 5 on insurance customer protection.
General Provisions	Part XVI (14) Intervention and remedial action Winding up -General provisions on winding up -Provisions specific to licensed Takaful operators -Priority of payments in winding up -General provisions in relation to actions taken by Bank	Chapter X (10) Dissolution, liquidation and bankruptcy Article 50 (1) (2) (3) Article 51 (1) (2) (3) (4) Article 52 (1) (2) (3) (4)	Not available	Discuss the details include general provisions, priority of payments and general provisions in relation to actions taken by bank and Takaful operators.
Penalty and Confinement	Part XVI (16) Enforcement and penalties i)Investigation powers ii)Administrative actions iii)Civil actions iv)Criminal offences v)General matters	Chapter XVI (16) Penalty provision Chapter XV (15) Administrative sanctions	Bab VIII (7) Administrative sanction (SANKSI)	Its include investigation powers, administrative actions, civil actions and criminal offences. It’s also provided under Chapter XV (15) under UU40. Its further explains under VIII (7) under POJK 23.

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General Provisions	Part XVII (17) i)Power of minister on regulations	Chapter XIII (13) REGULATIONS AND SUPERVISION	Not available	
Transitional Matters	Part XVIII (18) Repeal, saving and transitional i)Repeal, saving and transitional matter	Chapter XVII (17) Transitional provision Chapter XVIII (18) Closing	Bab VIII (8) Transitional provisions (ketentuan peralihan)	Any rule, regulation, order, notification or other subsidiary legislation made, and any approval, authority, consent, etc. before the ACT shall continue to remain in full force and effect about the person to whom it applied until amended or revoked

DIFFERENCES			
Criteria	**IFSA 2013 (Malaysia)**	**UU No 40 & POJK No 23 (Indonesia)**	
Islamic Money Market	Part X (10) Islamic money market and Islamic foreign exchange market i)Islamic money market	**UU No 40**	**POJK No 23**
		Not available - not related to Takaful sector	Not available
Submission	Part XI (11) Submission of document or information i)Details of submission document	Not available - not related to Takaful sector	Not available

Directions	Part XIII (13) Directions of compliance i)Circumstances where bank has the power to issue directions	Not available - not related to Takaful sector	Not available
Other Power of Bank	Part XV (15) Other power of bank i)Regulation of prescribed Islamic financial institutions ii)International and domestic transactions iii)Holiday for licensed person	Not available - not related to Takaful sector	Not available
Insurance Program	Not available	Chapter VIII (8) Mandatory insurance program	Not available
Business Association of Insurance	Not available	Chapter XIV (14) Business association of insurance	Not available
Regulation and Supervision	Not available	Chapter XIII (13) REGULATION AND SUPERVISION Article 61 (1) (2) (3) (4)	Chapter V (5)** BUSINESS CONDUCT (Article 22 and 23)
Examination	Part XII (12) i)Document submit examine by bank	Not available	Not available

CONCLUSION

Based on the above discussion, the countries in ASEAN had rules and regulations that provide by their regulator to protect the Takaful industry. The regulator is responsible for usually setting on a minimum capital requirement, the solvency regulation, policyholder protection and foreign ownership restrictions. It will open new opportunities in a rapid growth market, especially in Malaysia and Indonesia. Takaful rules and regulations are very critical to ensure sound Takaful operations in ASEAN countries. Regulations could reduce mismanagement, increase the level of solvency and strengthen a company's position in the face of global competition. The current general Takaful rules and regulations are IFSA 2013 in Malaysia and UU40 in Indonesia. However, UU40 referring to Takaful company and the conventional insurance company was more straightforward and only discuss on the headlines for insurance and takaful because the further explanation of it will be provided in the Peraturan Otaritas Jasa Keuangan (POJK). Whereas, IFSA 2013 referred to Takaful company covered all the Takaful rules and regulations and also compiled of banking, Takaful and money market. Inspire of making a comparison with regards to the general rules and regulations and more on administrative matters which referred to IFSA 2013 and UU40; it was suggested to compare the important operational matters also.

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